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NOTES AND MEMORANDA

FARMERS' MUTUAL FIRE INSURANCE IN MINNESOTA

FOR several years prior to 1875 a demand on the part of the farmers of the state of Minnesota for a law authorizing and outlining a plan for rural mutual insurance against loss by fire or lightning was making itself felt in the legislature. Several small companies of this nature were already in existence, the two earliest ones of which the writer has any knowledge being organized in 1867. These companies were desirous of legal recognition, and the farmers in various other communities were ready to organize as soon as an opportunity to incorporate on a legal basis had been provided.

To get such a law on the statute books, however, proved no easy matter. That the old line companies were not idle at such a time can readily be imagined. But the most outspoken enemy of the proposed plan was the Insurance Commissioner of the state. In the annual report ¹ of this officer for 1874 we are informed that in the legislative session of the previous year a bill was introduced providing for an "indiscriminate organization of Township Mutual Companies." The bill passed both houses of the legislature, but the signature of the governor, in the words of the Commissioner, "was prudently withheld." He further relates how in the legislature of the year of the report two further attempts were made to pass such a law, the bill in both cases being defeated in the Senate after passage by the House. Despite his warnings and arguments, in the following year, 1875, the legislature passed the

¹ Minnesota Insurance Report, Fire, 1874, p. 53, etc.

act authorizing the formation of Township Mutual Insurance Companies.

The experiment has been highly successful. The report for the year 1885 shows that, during the first ten years that the law was in operation, forty-three Township Mutuals had attained a working basis and were at the time of the report carrying an aggregate risk of over \$8,000,000. According to the report for 1910, there are 149 such companies in the state, with a total membership of 135,382, and with a total insurance on their books of \$254,018,393. By the strictly mutual plan of insurance at cost the farmers of Minnesota are saving themselves in insurance premiums about three quarters of a million dollars annually.

The law of 1875 has been amended from time to time, practically all the changes being in the nature of amplifications of the original provisions. The most thorough revision was undertaken by the Legislature of 1909, at the recommendation of the present Insurance Commissioner. The present law¹ provides that the number of incorporators shall be, as by the original act, twenty-five or more. But the amount of property which these incorporators must possess and offer to insure is raised to \$50,000 as a minimum, instead of \$25,000. The contingencies insured against remain the same, namely, fire or lightning. The incorporators must reside in adjacent towns, and it is further provided that no company shall operate in more than fifty towns at the same time. The certificate of incorporation, which by the statute is carefully outlined as to content, and a copy of the by-laws of the company are required to be filed with the Commissioner of Insurance, after approval and endorsement by him.

The number of directors is left as before, not less than five nor more than nine; but instead of being limited to a one-year term they may be elected for three years or less as the by-laws of the company shall provide. The directors are required to choose from among their number one president, one vice president, and one secretary. They

¹ General Laws of Minnesota, 1909, Chap. 411.

are also required to elect a treasurer who must be a member of the company, but need not be a member of the board unless the directors so desire. The treasurer is required to give bonds in such sum as the directors shall determine. A person owning property within a town in which a township mutual is authorized to operate may become a member of the company and insure his property so located, even tho his place of residence is not within such limits. A member may at any time withdraw from the company by proper notice to the secretary, and the payment of his share of all existing claims.

The kinds of property that may be insured have been enlarged by amendment on several occasions. The present law provides that the following kinds of property may be insured: "dwellings and their contents, farm buildings and their contents, live stock, farm machinery, hay, grain in the bin or stack, churches, school houses, society or town halls, country blacksmith shops and their contents, and the barns and contents used in connection therewith, butter makers' dwelling houses and contents, and barns and contents used in connection therewith." The companies are, as before, prohibited from insuring any property within the limits of any city or village, "except that located upon lands actually used for farming or gardening purposes." The term for which policies may be issued is, as in the original law, limited to five years. A company may take joint or partial risks with other companies, but no company may insure property already insured by another, except with the consent of the former insurer, nor may the total joint insurance exceed in value the sum for which such property is insurable by such former company. In cases of joint insurance, companies are not limited to the territory in which they are regularly authorized to do business. Classification of property is permitted, as to degree of risk.

Before issuing a policy the company is required to collect "regular cash premium and policy fee and take the written agreement of the insured . . . to pay pro rata share of all losses sustained by the company." The amount of such

cash premium is left to be determined by each organization for itself. To make doubly sure that assessments are collectible the act specifically states that suits at law may be brought against any member refusing or neglecting to pay such assessment. It is further provided that in case the directors wilfully neglect or refuse to perform the duties of their office in connection with a loss, they become, as under the original law, liable in their individual capacity to the person having the claim against the company.

All losses are required to be properly reported to the secretary, and if the claim involved exceeds \$300, the directors are required to appoint a committee of three members of whom the secretary shall be one. This committee has the power of examining witnesses and the secretary is authorized to administer oaths, in determining the amount of the loss. The by-laws, however, may provide that the secretary shall himself determine losses, and even without such provision, he and the president, or either of them, may pass upon all claims of \$300 or less. In case of failure to reach a satisfactory settlement under any of these provisions, the law requires that the matter shall be referred to an arbitration board, consisting of three disinterested men, one of whom is to be chosen by the company, one by the insured, and a third by the two so chosen. The award of a majority of these three is declared to be final unless an appeal be made to the courts. Such action by an arbitration board, however, is required, unless waived by mutual agreement, before action in court is permitted. The referees or arbitrators are allowed \$2.00 per day and a 5c. mileage. These charges, together with witness fees, if any, must be paid by the company if the award is higher than the sum offered by the officers or the original committee of the organization; if the award is not so increased, these expenses are borne by the claimant.

A company instead of waiting for a loss to occur may collect and maintain in its treasury a sum not to exceed two mills on each dollar insurance in force, or it may, after a loss has occurred, borrow a sum not to exceed the per-

centage above mentioned, and thus postpone an assessment. Funds in the treasury of the company may, with the authority of the directors, be loaned by the treasurer on first real estate securities, or upon similar authorization they may be deposited by him in banks approved by the directors.

The average amount of risk on the books of each of the 149 companies is a little over \$1,700,000. There are 59 companies having a total insurance in force of less than \$1,000,000. Many of these, of course, are but recently organized and have not had time to attain normal proportions. Forty-nine companies have each between one and two million dollars insurance in force; seventeen have between two and three million; twelve have between three and four million; eight have between four and five million, and four companies have each over five million.

No company, it will be recalled, is permitted to operate in more than 50 townships at the same time. Only one company has reached the legal limit in this respect. Three other companies operate in more than forty townships. Twelve companies operate in thirty or more but less than forty townships; thirty-six companies in twenty or more but less than thirty; sixty-five in ten or more but less than twenty; and thirty-two in less than ten townships. Thus it is seen that ninety-seven, or almost two-thirds of the companies, limit their respective fields of operation to less than twenty townships, while only sixteen, or one-tenth of the companies, operate in thirty or more townships each. It would appear from these figures, as well as from other computations that may be made, that the favorite area for a company to take in as business territory is fifteen to twenty townships. The largest company operates in but twenty-one townships. Two of the other companies having a business in excess of \$5,000,000 operate in twenty townships each, while the fourth company in the same class operates in thirty-six such units of area. No company operates in less than two townships, and but one company is confined to two. There are but five companies, all told, restricted to less than five townships each. Fifty-six of

the companies have their territories all in the same county, and, strangely enough, three of these are in the "five million" group. Thirty-four companies have their territory in two counties; thirty-five in three counties; eighteen in four counties, and six in five counties. Whether or not the townships in which a company by its charter is allowed to do business are within the limits of one or more counties will depend, of course, very largely upon the domicile of the company with reference to county lines.

It cannot be doubted that difference of nationality and even church affiliations have played a considerable part in forming the boundaries of many of the companies. Happily, this tendency seems to be rapidly waning as Minnesota citizens from different parts of the country, and more especially from different foreign countries, learn to understand one another through the use of a common language and the discovery of common interests. No more striking example of this process could well be given than the history of one of these insurance companies formed by a colony of foreign-born citizens before the law of 1875 gave legal sanction to such an organization. As first organized, membership was restricted both by nationality and church. Within a year both qualifications were partially removed, tho the changed name was still written in the foreign language of the founders. Four years later the organization became a "Farmers' Mutual Insurance Club" and today, under the name of the township of its official domicile, it is one of the 149 companies we are discussing.

The companies have doubtless done much to create among the farmers of Minnesota a feeling of fellowship and a community of interest. This is stimulated by the annual and other local meetings of the membership of each individual company, and by an annual gathering of representatives organized in a state association. The fifteenth annual meeting of the association was held at St. Paul on the twelfth and thirteenth of last January. Sixty-two companies were represented. Some of the topics discussed were blanks, books and bookkeeping, proper

initial premium rates, proper amount of reserve funds and the disposal of these until needed, classification of risks, and proper valuation of high-priced stock on the farm. In the discussion of reserve funds, for instance, it was shown that a decided saving could be accomplished by charging a large enough premium upon the issuing of a policy to avoid making an assessment except upon extraordinary occasions. The practice in this respect is at present, however, very divergent. Initial premiums vary in different companies from ten cents per hundred dollars to seventy-five cents, for a five-year policy. Experience shows that by charging the latter figure, assessments, each of which cost an average company some \$200 or \$300, can be almost entirely avoided. A majority of the members present favored a reserve of something over \$1,000 for a company having about \$1,000,000 insurance in force, the percentage of reserve decreasing as the company's insurance in force exceeded that amount. Such discussions are of great value to men who, with all their sturdy virtues, are often deficient in knowledge of the corporate way of doing things, and of business methods and accounts.

The moral hazard, from the very nature of an organization with neighborhood control, is less than with stock companies, or even with mutual companies doing a more general business. It is further reduced by the practice of refusing to insure for more than two-thirds or at most three-fourths of the actual value of the property. The similarity of the risks of these companies, and the knowledge of neighbors as to the condition and value of the property of an applicant for insurance make it possible to apply this rule without difficulty. Commissioner Elmer H. Dearth, in his report for the year 1901, makes the rather sweeping assertion¹ that the township mutuals have entirely eliminated the moral hazard, and finds the cause in the fact that each member feels himself part and parcel of the company.

In addition to eliminating the moral hazard, or at least in greatly reducing it, the companies have accomplished

¹ Minnesota Insurance Report, Fire, 1901, p. xxii.

something in the way of reducing the number of accidental fires. Most of their by-laws contain numerous precautions which must be observed by the insured. Among these are the placing of all hay or straw stacks beyond a specified distance from any building wherein fire is used, always having on hand certain fire fighting apparatus, such as water pails, a ladder of sufficient height, and other appliance by which the ridge of the roof may be reached, etc. Stove pipes and chimneys are required to be in good repair and proper non-conducting thimbles used where pipes pass through partitions, ceilings, or roof. Endangering buildings by the careless disposal of hot ashes is usually provided against. If these precautions are not observed, then, in the words of the by-laws of one of these companies, "the insured shall not be entitled to any insurance to the extent that such loss or damage has been caused or increased by such violations." In securing the observance of these precautions, as in guarding against over-insurance and the consequent moral hazard, these local and consciously mutual organizations have a decided advantage over the larger and more complex old line companies.

In the thirty-five years since the beginning of the movement, not a single company has failed to meet its obligations. Two partially organized companies, it is true, failed to enter on business; but every company fully organized has been a success. Commissioner Dearth, speaking before the National Association of Coöperative Insurance Companies which met at St. Paul in 1902, after pointing out the remarkable success of the Township Mutuals of Minnesota, pays them the following tribute: "These companies deserve the greatest consideration, not only for the very large policy or membership, but on account of the thoroly earnest, conscientious, and conservative management which has been a marked characteristic of their business transactions." He calculates that the average cost of insurance to the farmers in their own companies, about seventeen cents per hundred — thirteen cents of which covers losses and four cents expenses, — is about one-fifth what it would

have cost them in old line companies, and that the Township Mutuals saved the farmers of the state in the year 1901 alone \$1,069,000, and up to that date had saved a total sum of not less than \$12,000,000. "Old line joint stock companies," he asserts, "find it unprofitable to carry these risks even at a rate of seventy-five cents or a dollar, and such as had a farm department formerly are withdrawing from the field." The last part of this statement is borne out by an inquiry as to the number of stock companies represented by the leading local fire insurance agencies who at present insure farm property. It would seem, however, that in estimating the difference in cost to the farmers under the two plans, the Commissioner has used the one year rate for the stock companies, instead of one-third of their three years' rate, which would more accurately represent true cost to the insured; it being the established rule to give three years' protection at twice the annual rate.

The actual amount that the Township Mutuals are saving the farmers annually is perhaps impossible to estimate, since no one can say just to what extent the present rates quoted by stock companies — in so far as they still offer rates — have been influenced. Taking their rates as quoted at the present time, the annual saving, tho not so great as might be inferred from the figures of Commissioner Dearth, is still very considerable. The present rate by such stock companies as take farm risks varies from sixty-five cents per hundred for one year and \$1.25 for three years, to seventy-five cents for one year and \$1.50 for three. The higher rates are applied to the more sparsely as well as more newly settled northern parts of the state. Under the three-year plan, the average annual cost to farmers insuring in stock companies would be about a third of \$1.375, or forty-six cents per hundred. The average cost in the Township Mutuals is about seventeen cents per hundred, — an annual saving of twenty-nine cents per hundred of insurance. At this rate, with over \$254,000,000 insurance in force, the Township Mutual companies

saved the farmers of the state in the year 1909 about \$750,000. The total savings during the third of a century that the system has been in operation would amount to more than ten million dollars. Were we to allow for the effect of competition in reducing the rate of the old line companies, and for compound interest on the premium charges saved from year to year, these figures would probably be doubled.

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THE POSITION OF INCOME BONDS, AS ILLUSTRATED BY THOSE OF THE CENTRAL OF GEORGIA RAILWAY

INCOME bonds have owed their existence to periods of financial embarrassment. During the long series of successive railway reorganizations which culminated in the nineties, the purpose of every endeavor which looked toward the rehabilitation of a bankrupt property was to decrease the immediate fixed charges. This was accomplished usually by compelling the holders of junior mortgages to accept obligations which involved no fixed rate of interest and no foreclosure rights because of default in interest payments. Interest or dividend on this new class of securities would be paid only if earned. Assessments on stock and consolidated mortgages were funded by the issuance of the same kind of security. This whole method of financing involved the formation of a new class of securities intermediate in character between the prior lien bonds and the common stock. It also involved the entire readjustment in the kind of securities represented in the liability account, with usually an increase in the par value of the junior issues and a slight but not corresponding decrease in the interest-bearing bonds. As a result of this shifting the majority of railway companies emerged from reorganiza-